The New York Times
Prescriptions
Making Sense of the Health Care Debate

JANUARY 7, 2010, 2:46 PM

What Counts Toward the Cadillac Tax

By MICHELLE ANDREWS

President Obama apparently has embraced the so-called Cadillac tax, an excise tax on high-priced health insurance plans, urging its inclusion in the final health care legislation to be hammered out between Democratic leaders in the House and Senate.

But that Cadillac may be holding more than many consumers realize.

As envisioned in the Senate bill, an excise tax of 40 percent would be imposed on the value of individual health plans over $8,500 annually and family coverage over $23,000. What's less commonly known is that those dollar maximums include not just the premiums paid by employers and employees for medical insurance, but also for vision and dental coverage, as well as reimbursements from flexible spending accounts and health reimbursement arrangements, and employer contributions to health savings accounts.

If an individual were to withdraw $2,000 from a flexible spending account to help pay for medical care, for example, that amount would count toward the $8,500 ceiling. The employee isn't technically on the hook for the tax, which would be levied on the employer or health plan administrator. But experts agree that the tax will be passed along one way or another to the employee, perhaps through higher premiums, lower wages or cuts in other benefits.

"If you're contributing to one of those plans, your contributions will be subject to that excise tax, which presumably will be passed on to you as an employee," said Ken Sperling, who leads the health care reform team at the benefits consultant Hewitt Associates.

That contributions to tax-deferred plans could wind up being taxed "kind of eliminates the point" of contributing in the first place, Mr. Sperling added.

Flexible spending accounts in particular seem destined to become less attractive, even if the Cadillac tax isn't passed. The accounts, which are offered by more than 80 percent of large employers, allow employees to set money aside on a pretax basis to pay for medical expenses like co-payments, deductibles and over-the-counter drugs.

Currently there is no legal limit on the amount that an employee can deposit in such an account, though many employers set an annual cap at $5,000, said Paul Fronstin, director of the health research and education program at the Employee Benefit Research Institute, a private, nonpartisan group.

Under the House and Senate bills, however, the maximum annual contribution would be limited to $2,500. In addition, the bills would no longer allow people to be reimbursed for over-the-counter drugs unless they were prescribed by a doctor. This may be frustrating for people who use their flexible spending accounts for incidentals like aspirin and Band-Aids.

The drug-reimbursement restrictions would also apply to other tax-advantaged employee accounts like health savings accounts and health reimbursement arrangements.

Still, surprisingly few people would be affected by the changes to flexible spending accounts. Although people who take medication regularly or those who are expecting a hefty one-time medical expense, like paying for braces, may feel the pinch of lower contribution maximums, the average account contribution was just $1,380 in 2008, according to Mr. Fronstin’s research.

What’s more, only about 20 percent of people who are eligible to participate in a flexible spending account do so, Mr. Fronstin said. “Most of the population is healthy and uses very little health care,” he said.

Copyright 2010 The New York Times Company | Privacy Policy | NYTimes.com 620 Eighth Avenue New York, NY 10018